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Aqua Illinois, Inc.

Woodhaven Sewer Division

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INDEPENDENT ACCOUNTANTS' REPORT

To the Board of Directors
Aqua Illinois, Inc.

We have examined the accompanying Projected Statements of Utility Operating Income for the years ending December 31, 2005 and 2004, the Projected Statements of Jurisdictional Rate Base as of December 31, 2005 and 2004 of Aqua Illinois, Inc. - Woodhaven Sewer Division, and the Projected Statements of Capital Structure as of December 31, 2005 and 2004 of Aqua Illinois, Inc. Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the projected financial information, except for the Statement of Capital Structure, which was limited to the activity of the Woodhaven Sewer Division.

The accompanying projected financial information presents, to the best of management's knowledge and belief, the Projected Statements of Utility Operating Income for the years ending December 31, 2005 and 2004, and the Projected Statements of Jurisdictional Rate Base as of December 31, 2005 and 2004 of Aqua Illinois, Inc. - Woodhaven Sewer Division, and the Projected Statements of Capital Structure as of December 31, 2005 and 2004 of Aqua Illinois, Inc. that would result if the wastewater rates in effect during 2003 would not change prior to December 31, 2005 as discussed in note 3.

The projected financial information and this report were prepared in connection with an application to the Illinois Commerce Commission by the Company for an increase in sewer rates for the Woodhaven Sewer Division and should not be used for any other purpose. The Illinois Commerce Commission requires the use of a projection based on the assumption that there will be no rate increase during the projection period.

In our opinion, the Aqua Illinois, Inc. - Woodhaven Sewer Division Projected Statements of Utility Operating Income for the years ending December 31, 2005 and 2004 and the Projected Statements of Jurisdictional Rate Base as of December 31, 2005 and 2004 presents fairly, in conformity with the guidelines for a presentation of projected information established by the American Institute of Certified Public Accountants and the underlying assumptions provide a reasonable basis for management's projection given the hypothetical assumption that rates in effect during 2003 would not change prior to December 31, 2005 as discussed in note 3. However, even if such hypothetical assumption were to occur, there will usually be differences between projected and actual results because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

London Witte Group, LLC

December 15, 2004

Certified Public Accountants

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Aqua Illinois, Inc.
Woodhaven Sewer Division Only

PROJECTED STATEMENTS OF UTILITY OPERATING INCOME

For the Years Ending December 31, 2005 and 2004

	Woodhaven Sewer Division	
	<u>2005</u>	<u>2004</u>
OPERATING REVENUE	\$ <u>750,585</u>	\$ <u>804,118</u>
OPERATING EXPENSES		
Operation and maintenance	541,939	464,851
Depreciation and amortization	90,631	84,432
Taxes on operating income -		
General	41,650	87,956
State income	(26,016)	44,470
Federal income	(5,055)	9,123
Amortization of investment tax credit	0	0
Total Operating Expenses	\$ <u>643,149</u>	\$ <u>690,832</u>
UTILITY OPERATING INCOME	\$ <u><u>107,436</u></u>	\$ <u><u>113,286</u></u>

See accompanying summary of significant projection assumptions and accounting policies.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

PROJECTED STATEMENTS OF JURISDICTIONAL RATE BASE

December 31, 2005 and 2004

	Woodhaven Sewer Division	
	<u>2005</u>	<u>2004</u>
GROSS UTILITY PLANT IN SERVICE AT ORIGINAL COST	\$ 6,229,185	\$ 6,064,947
LESS: Reserve for accumulated depreciation and amortization	<u>2,049,244</u>	<u>1,953,739</u>
NET UTILITY PLANT IN SERVICE	4,179,941	4,111,208
PLUS:		
Amortization of CIAC	537,309	512,709
Working capital allowance	64,453	64,834
Deferred charges	32,615	36,415
Materials and supplies	8,218	8,105
LESS:		
Customer advances	184,207	184,207
FAS 87 pension	27,365	17,123
Contributions in aid of construction	1,232,939	1,220,189
Deferred income tax	<u>411,556</u>	<u>412,825</u>
PROJECTED JURISDICTIONAL RATE BASE	\$ <u>2,966,469</u>	\$ <u>2,898,927</u>

See accompanying summary of significant projection assumptions and accounting policies.

Aqua Illinois, Inc.

PROJECTED STATEMENTS OF CAPITAL STRUCTURE

December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
LONG TERM DEBT	\$ 57,216,655	\$ 57,054,325
SHORT TERM DEBT	0	1,800,000
PREFERRED STOCK	382,372	382,372
COMMON EQUITY	<u>63,413,016</u>	<u>59,303,179</u>
Total	<u>\$ 121,012,043</u>	<u>\$ 118,539,876</u>

See accompanying summary of significant projection assumptions and accounting policies.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

(1) INTRODUCTION

This projected statement's of utility operating income for the years ending December 31, 2005 and 2004, the projected statements of jurisdictional rate base and the projected statements of capital structure as of December 31, 2005, and 2004 (Projected Financial Information), to the best of management's knowledge and belief, reflect the projected rate base and operating income for the years to end December 31, 2005, and 2004 of Aqua Illinois, Inc. for the Woodhaven Sewer Division (the "Company"), a wholly owned subsidiary of Aqua Illinois Water, Inc., and the projected capital structure of Aqua Illinois Water Company as of December 31, 2005 and 2004, assuming no change prior to December 31, 2005, in sewer rates from those rates in effect during 2003. Accordingly, the Projected Financial Information reflects management's judgment as of December 2004, the date of this Projected Financial Information, of the expected conditions and its expected course of action assuming no change prior to December 31, 2005, in sewer rates. The Illinois Commerce Commission requires the use of a projection based on the assumption that there will be no rate increase during the projection period.

Projections for 2004 were from budgeted numbers generated and updated in the first half of 2004. No adjustments were made to reflect specific transactions occurring during 2004.

The Projected Financial Information was prepared in connection with an application to the Illinois Commerce Commission ("ICC") by the Company for increases in sewer rates and should not be used for any other purpose. The assumptions disclosed herein are those that management believes are significant to the Projected Financial Information. Even if there is no change in sewer rates from those in effect during 2004, there will usually be differences between projected and actual results because events and circumstances frequently do not occur as expected, and those differences may be material.

(2) SIGNIFICANT ACCOUNTING POLICIES

The Company's accounting policies used in the preparation of this Projected Financial Information are in conformity with generally accepted accounting principles for regulated public utilities and accounting procedures prescribed by the ICC. The Company follows the provisions of Statement of Financial Accounting Standards ("SFAS") No. 71, which provides guidance for the preparation of financial statements of companies in regulated industries.

Property, Plant and Equipment

The cost of additions to utility plant and replacement of retired units of property is capitalized. Cost includes material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. Repairs, maintenance and minor replacements of property are charged to current operations. The cost of property units retired in the ordinary course of business plus removal cost (less salvage) is charged to accumulated depreciation.

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Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

(2) SIGNIFICANT ACCOUNTING POLICIES (continued)

Additions to utility plant (net of retirements) were projected based on the Company's capital investment plan, excluding allocated corporate additions and amortization of acquisition adjustments, are \$94,501 for 2005 and \$799,224 for 2004.

For financial reporting purposes, depreciation is computed on the straight-line method over the estimated service lives of the assets as approved by the ICC. For income tax reporting purposes, depreciation is computed using applicable tax reporting guidelines (primarily accelerated methods).

Allowance for Funds Used During Construction

The allowance for funds used during construction ("AFUDC") represents the estimated cost of funds used to finance the construction of utility plant. AFUDC is applied to construction projects requiring more than two months to complete. No AFUDC is applied to projects funded by customer advances for construction or contributions in aid of construction. AFUDC includes the net cost of borrowed funds and a rate of return on other funds when used, and is recovered through water rates as the utility plant is depreciated.

Regulatory and Other Long-Term Assets

Unamortized debt issuance expense is amortized over the life of the related debt issue.

Amortization of contributions in aid of construction is recorded using the appropriate depreciation rate for depreciable mains in service at December 31, 2003.

Recognition of Revenues

Sewer service revenues for financial reporting purposes include amounts billed to customers on a cycle basis and unbilled amounts determined using estimated usage and rates, from the date of the latest meter reading to the end of accounting period.

Employee and Postretirement Benefits

The Company has a defined benefit pension plan covering substantially all of its employees. Pension benefits are based on years of service and the employee's average salary during the last five years of employment. The Company's funding policy is to contribute an amount that will provide for benefits attributed to service to date and for those expected to be earned in the future by current participants to the extent deductible for income tax purposes.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

Employee and Postretirement Benefits (continued)

In addition to pension benefits, employees retiring from the Company in accordance with the retirement plan provisions are entitled to postretirement health care and life insurance coverage. These benefits are subject to deductibles, co-payment provisions and other limitations. The company may amend or change the plan periodically. In 1997, the Company established a Voluntary Employee Benefit Association.

The Company has adopted the delayed recognition method under which the unrecorded SFAS No. 106 liability as of January 1, 1993, will be amortized to expense on a straight-line basis over a 20-year period.

Dividends

Aqua Illinois, Inc. has projected annual dividend payments of \$20,939 to its preferred stockholders in 2004, and \$20,939 in 2005. In addition, the projected common stock dividend for 2004 is \$1,585,149.

(3) HYPOTHETICAL ASSUMPTIONS

Sewer rates

The preparation of the Projected Financial Information is based on the assumption that the sewer rates in effect during 2003 will not change prior to December 31, 2005.

The purpose of the Projected Financial Information is to reflect sewer rates in effect pursuant to the Company's most recent rate order and the Company's projected cost of service for the year ending December 31, 2004. Such information will then be included in the Company's application for an increase in sewer rates. The Illinois Commerce Commission requires the use of a projection based on the assumption that there will be no rate increase during the projection period.

(4) OPERATING REVENUES

Projected operating revenues are derived by applying the sewer rates in effect during 2003 to current and historical water consumption trends adjusted for expected changes in the number and mix of customers during 2005 and 2004. For the residential and commercial customer classes, the number of customers in each class for the forecast period was determined by adjusting the 2003 year end number of customers by the average annual rate of customer growth or decline. Average consumption per customer for 2003 was utilized. For the industrial customer class, customer numbers were held constant at the 2003 year end level. Any known changes in industrial customers, or changes in consumption levels for existing customers, were figured into the revenue calculations. Historical data on consumption is used to determine price per 1,000 gallons. The growth in consumption multiplied by consumption price results in the projected revenue. Decreases in revenue for 2005 result from the Company more closely monitoring the accounts of delinquent customers.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

(5) OPERATING AND MAINTENANCE EXPENSES

As presented in the following assumptions, operating and maintenance expense items have been projected based on a number of factors. For those areas where firm bids have not been received or other pertinent information is not available, management expects the cost escalator rate to be 3% for the years ending December 31, 2005 and 2004. Where appropriate, this cost escalator rate was used in the development of operating and maintenance expense amounts.

Significant components of operating and maintenance expenses include the following:

A. Salaries, Wages and Employee Benefits

The company has salaried, union hourly wage positions, and part-time hourly employees. All employees are paid on a bi-weekly system. Wage and salary increases are projected for 2005 based on inflationary factors plus employee performance. Employee insurance premiums are projected based on insurance contracts in place for the year ended December 31, 2004. 2005 wage and salary increases are based on union contracts or 3.5% with a 1% increase in employee benefits due to health benefits over the 2004 projected numbers.

B. Chemicals

Projected chemical expense is based on historical costs for each major chemical and the usage of that chemical as a function of consumption. The 2003 usage and expense rates were then applied to the projected water consumption for 2005 and 2004. The forecasted expenses were adjusted 3% for 2005.

C. Material and Supplies

Materials and supplies for 2004 are projected to remain constant with 2003, and increase by the 3% inflation rate for 2005 over 2004.

D. Contractual Services

These services include allocations from Aqua Illinois, Inc. and Aqua America, Inc. for costs such as customer services, administrative personnel, insurance, computer services, engineering, operations and regulatory practices. These expenses are allocated to each division based on equivalent customers for that division. Company management believes the use of equivalent customers approximates the amount of support the division will receive from the Company's corporate structure. Outside contractor expense was projected based upon historical expenses and needs foreseen for the years 2004 and 2005. Accounting services included a portion for the year-end audit, estimated and provided by Aqua America.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

D. Contractual Services (continued)

Legal services were calculated based on the 5 years of historical spending with the high and low year eliminated and the remaining 3 years averaged. The calculated average was reduced by 50% for the shifting of legal work from outside contractors to Aqua America legal staff. Other legal fees were then adjusted to reflect forecasted changes in legal services required for specific matters. Laboratory expenses were projected to be consistent with the historical level of service used, with a 3% price increase projected for 2005.

E. Transportation Expense

Maintenance transportation expense has been forecasted using historical data for maintenance and repairs to forecast the level of expenditures for 2004, adjusted for an increase of 3% for 2005.

F. Insurance Expense

Workers' compensation insurance and general liability insurance are projected based on current premiums adjusted for increase premiums of 7.31% for the year 2005.

G. Uncollectible Expense

Based upon an analysis of the historical period of 2002 and 2003, average ratios of annual write-offs as a percentage of annual revenues were established. Projected uncollectible expenses was calculated by applying the established average write-off and collection ratio to the projected annual revenue figures.

H. Miscellaneous Expenses

These expenses are primarily composed of postage, telephone, court costs and other administrative and general expenses. A review of historical information provided guidelines for calculation of itemized projections for 2004 and 2005.

I. Depreciation Expense

Utility plant additions and retirements included for purposes of calculating the projected depreciation expense for 2005 are based on the Company's capital investment projections.

J. Corporate Expense Allocation

Corporate operating expenses are allocated to divisions based upon number of customers. During 2005 the calculation used for number of customers changed, resulting in a higher allocation to the Woodhaven Sewer Division.

Aqua Illinois, Inc.
Woodhaven Sewer Division Only

SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

(6) TAXES ON OPERATING INCOME

General Taxes

General taxes consist of real estate property taxes, invested capital taxes, payroll taxes and miscellaneous taxes.

The projected general taxes expense includes the additional property tax base resulting from projected plant additions, projected increased labor costs and increases in invested capital. Real estate property tax projections are based on the most current reassessments and a 2% increase in rates for 2005 and 2004. Investment capital taxes are calculated for the total company and then allocated to each division. The allocation of these taxes was based on number of customers for 2004 and utility plant for 2005. This resulted in a decrease in investment capital taxes between 2004 and 2005.

Federal and State Income Tax

Accounting for income taxes requires an asset and liability approach for financial accounting and reporting. The Company is required to establish deferred tax assets and liabilities as appropriate, for all temporary differences and to adjust deferred tax balances to reflect changes in tax rates expected to be in effect during the period the temporary differences reverse. Temporary differences occur because the income tax law either requires or permits certain items to be reported on the Company's income tax return in a different year than they are reported in the financial statements.

Investment tax credits have been deferred and are being amortized to income over the life of the property-giving rise to such credits.

The Company is included in the consolidated income tax returns of Aqua America, Inc.. Income taxes in these financial projections have been determined as if the Company prepared its tax returns on a stand-alone basis.

For purposes of this rate case, the deferred income tax expenses have been projected on a company-wide basis and then allocated to each division. The allocation factor is the individual division portion of the asset or liability giving rise to the deferred tax amount.

The primary reason for the difference between the expected federal income tax expense at the statutory rate of 35% for federal and 7.18% for state income tax expense included in the projected statement of utility operating income results principally from amortization of investment tax credits and the reversal of excess deferred taxes.

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SUMMARY OF SIGNIFICANT PROJECTION ASSUMPTIONS AND ACCOUNTING POLICIES
For Years Ending December 31, 2005 and 2004

(7) CUSTOMER ADVANCES FROM CONSTRUCTION AND CONTRIBUTION IN AID OF CONSTRUCTION

Projected contributions in aid of construction assumes projects financed by customer advances and contributions are completed in the year the funds are received and that advances and contributions will approximate the projected construction costs required to complete the project. Accordingly, projected customers advances and contributions are credited directly to contributions in aid of constructions and the related depreciation on the contributed property is also charged to contribution in aid of construction.